

## Message Text

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ACTION AF-10

INFO OCT-01 ISO-00 SP-02 ICA-11 AID-05 EB-08 NSC-05

TRSE-00 SS-15 STR-07 OMB-01 CEA-01 CIAE-00

COME-00 FRB-03 INR-10 NSAE-00 XMB-02 OPIC-03

LAB-04 SIL-01 AGRE-00 DOE-15 SOE-02 /106 W

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R 280739Z AUG 78

FM AMEMBASSY PRETORIA

TO SECSTATE WASHDC 2292

INFO AMCONSUL CAPE TOWN POUCH

AMCONSUL DURBAN POUCH

AMEMBASSY GABORONE

AMCONSUL JOHANNESBURG POUCH

AMEMBASSY MASERU

AMEMBASSY MBABANE

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E.O. 11652: N/A

TAGS: ECON, EFIN, SF

SUBJECT: HIGHLIGHTS AND DISCUSSION OF RESERVE BANK ANNUAL REPORT

SUMMARY: ANNUAL REPORT OF RESERVE BANK AND GOVERNOR'S ADDRESS PROVIDED PICTURE OF AN ECONOMY GRADUALLY EMERGING FROM RECESSION AND WITH BALANCE OF PAYMENTS CONTINUING TO SHOW MODERATE IMPROVEMENT. SPECIAL FACTORS HAVE, HOWEVER, MADE IT DIFFICULT TO JUDGE STRENGTH OF RECOVERY TO DATE. RESERVE BANK REPORTS REAL GDP FOR YEAR ENDING JUNE 30, 1978 SHOWED SLIGHT DECLINE BUT GREW AT 3.5 PERCENT ANNUAL RATE IN FIRST HALF OF 1978. SECOND QUARTER OF 1978 SAW GROWTH AT ABOUT 8 PERCENT ANNUAL RATE, HIGHEST QUARTERLY RISE IN THREE YEARS. HOWEVER, FIGURES FOR QUARTER WERE INFLATED BY SURGE OF CONSUMER BUYING PRIOR TO INTRODUCTION OF 4 PERCENT RETAIL SALES TAX SO THAT ACTUAL EXTENT OF RECOVERY REMAINS UNCLEAR. CURRENT ACCOUNT SURPLUS IN 1977/78 OF ABOUT ONE BILLION RAND WAS COUNTERBALANCED BY EQUIVALENT OUTFLOW OF CAPITAL. IN FIRST TWO

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QUARTERS OF 1978, CONTINUED LARGE CURRENT ACCOUNT SURPLUSES OF OVER ONE BILLION RAND ANNUAL RATE (SEASONALLY ADJUSTED) WERE REPORTED. WITH CAPITAL OUTFLOW DOWN SOMEWHAT, A SMALL INCREASE IN THE CRUCIAL NET RESERVES OCCURRED IN FIRST HALF OF 1978. CONTINUING GOVERNMENT POLICY OF LIMITED STIMULUS, RESERVE BANK GOVERNOR DE JONGH ANNOUNCED LOWERING OF BANK RATE FROM 9 PERCENT TO 8.5 PERCENT AND REDUCTION IN LIQUID ASSET REQUIREMENTS FOR SMALLER

BANKS. FIXED DOLLAR/RAND LINK WAS REAFFIRMED. END SUMMARY.

1. ON AUGUST 22, GOVERNOR T.W. DE JONGH PRESENTED THE ANNUAL REPORT OF THE SOUTH AFRICAN RESERVE BANK FOR THE YEAR ENDING JUNE 30, 1978. THE FOLLOWING ARE HIGHLIGHTS OF THE REPORT AND GOVERNOR'S ADDRESS AS WELL AS EMBASSY COMMENT.

2. NATIONAL ACCOUNTS: THE ANNUAL REPORT SHOWED THAT THE ECONOMY AFTER SPENDING CONSIDERABLE TIME AT THE DEPTH OF A RECESSIONARY CURVE HAS TURNED GRADUALLY UPWARD IN THE FIRST HALF OF 1978. FOR THE YEAR 1977/78 AS A WHOLE, REAL GROSS DOMESTIC PRODUCT DECLINED BY ONE-FOURTH OF ONE PERCENT. HOWEVER, REAL GROWTH CLIMBED TO A 3.5 PERCENT RATE IN THE FIRST SIX MONTHS OF 1978 AND AROUND 8 PERCENT IN THE SECOND QUARTER. UNDER NORMAL CONDITIONS, THIS WOULD BE EVIDENCE OF FAIRLY SUBSTANTIAL RECOVERY. HOWEVER, MOST OF THE GROWTH IN 1978 CAME FROM HIGHER EXPORTS AND INCREASED SALES OF CONSUMER DURABLES AND AT LEAST A PORTION OF THE LATTER REPRESENTED ANTICIPATORY BUYING TO BEAT THE NEW 4 PERCENT SALES TAX WHICH TOOK EFFECT JULY 3. THUS, IT IS STILL UNCLEAR HOW STRONG THE RECOVERY IS AND WHETHER THE GROWTH IN CONSUMER SPENDING REPRESENTS A SUSTAINED TREND. DE JONGH STATED CAUTIOUSLY THAT, "THUS FAR THE RECOVERY HAS BEEN SLOW TO GAIN MOMENTUM ALTHOUGH THERE IS EVIDENCE OF A MILD REVIVAL." MOST ECONOMIC INDICATORS, INCLUDING VOLUME OF MANUFACTURING PRODUCTION, IMPORTS, AND CAR SALES, WERE UP MODERATELY IN THE FIRST HALF OF 1978.

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3. BALANCE OF PAYMENTS: ANNUAL REPORT STATES CURRENT ACCOUNT SURPLUS OF R938 MILLION (R1.00 EQUALS \$1.15) WAS POSTED IN 1977/78. IT DOES NOT GIVE ACTUAL QUARTERLY BREAKDOWN BUT LISTS SURPLUSES AT SEASONALLY ADJUSTED ANNUAL RATE OF R1,256 MILLION IN THE FIRST QUARTER OF 1978 AND AN ONLY SLIGHTLY LOWER R1,098 MILLION IN THE SECOND QUARTER. BASED ON THE SEASONALLY ADJUSTED QUARTERLY FIGURES, THE CURRENT ACCOUNT IS PERFORMING WELL IN 1978 AND THE SURPLUS COULD SURPASS THAT OF 1977. HOWEVER, SEASONAL ADJUSTMENT IS AN IMPRECISE SCIENCE, AND THE TOTAL SURPLUS FOR REPORTING YEAR 1977/78 OF R984 MILLION SEEMS TOO LOW GIVEN ALREADY PUBLISHED FIGURES FOR THE FIRST THREE QUARTERS OF THE YEAR. THUS, AS WITH THE GDP FIGURES, THE DIRECTION BUT NOT THE STRENGTH OF THE TREND IS CLEAR FOR THE SECOND QUARTER OF 1978. THE CAPITAL ACCOUNT FOR 1977/78 SAW A NET OUTFLOW OF R1,064 MILLION OFFSETTING THE CURRENT ACCOUNT SURPLUS. RESERVE BANK REPORTS OUTFLOW DECLINED IN SECOND QUARTER OF 1978 FROM LEVEL OF FIRST QUARTER. NET FOREIGN EXCHANGE RESERVES INCREASED BY ABOUT R50 MILLION IN BOTH QUARTERS OF 1978 WHICH INDICATES A SLOW BUT STEADY IMPROVEMENT IN OVERALL BALANCE OF PAYMENTS POSITION.

4. LABOR: TOTAL NON-AGRICULTURAL EMPLOYMENT DECLINED BY ABOUT 1 PERCENT IN THE NINE MONTHS ENDING MARCH 1978. A SLIGHT UPTURN

IN EMPLOYMENT WAS REPORTED IN THE FIRST QUARTER OF 1978 AS WELL AS SLIGHT REDUCTION IN THE NUMBER OF REGISTERED UNEMPLOYED AMONG WHITES, COLOREDS, AND ASIANS.

5. PRICES: CONSUMER PRICE INDEX IS REPORTED TO HAVE INCREASED BY 10 PERCENT IN 1977/78 COMPARED TO 11.4 PERCENT IN 1976/77. PRICE INCREASES DROPPED NOTICEABLY IN FIRST TWO QUARTERS OF 1978 TO 9.1 PERCENT AND 5.1 PERCENT ANNUAL RATE RESPECTIVELY. HOWEVER, THE SECOND QUARTER FIGURE WAS DISTORTED BY VARIOUS TAX CUTS PRIOR TO INTRODUCTION OF SALES TAX AND MUST BE VIEWED AGAINST FACT THAT CONSUMER PRICES JUMPED A FULL 4 PERCENT IN JULY ALONE AS A RESULT OF THE SALES TAX. THUS, NO MAJOR IMPROVEMENT IN THE INFLATION RATE IN 1978 APPEARS LIKELY.

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6. MONETARY SITUATION: MONEY AND NEAR MONEY SUPPLY INCREASED BY 7 PERCENT DURING 1977/78 COMPARED TO 6 PERCENT THE PREVIOUS YEAR. THIS REAL DECLINE WHEN COMPARED TO 10 PERCENT INFLATION RATE WAS A MAJOR FACTOR IN RECESSION. HOWEVER, MONEY SUPPLY JUMPED SHARPLY TO 18 PERCENT ANNUAL RATE IN SECOND QUARTER OF 1978 TO FINANCE SURGE IN CONSUMER SPENDING, AND REFLECTED EASING OF GOVERNMENT'S TIGHT MONEY POLICY. SHORT-TERM INTEREST RATES WERE UNDER DOWNWARD PRESSURE IN MOST OF 1977/78 WHICH THE RESERVE BANK RESISTED WITH OPEN MARKET OPERATIONS.

7. STOCK MARKET: SHARE PRICES ON JOHANNESBURG EXCHANGE RECOVERED SIGNIFICANTLY IN 1977/78 WITH SHARE AVERAGE IN JUNE 1978 STANDING 30 PERCENT ABOVE JUNE 1977. GOLD SHARES SHOWED LARGEST GAINS, BUT INDUSTRIALS WERE ALSO UP. NOTABLE TREND WAS A MODERATE INCREASE IN VALUE OF SHARES HELD BY FOREIGNERS PARTICULARLY COMPARED TO 1976.

8. NEW POLICY MEASURES: DE JONGH ANNOUNCED THAT PURSUANT TO GOVERNMENT'S POLICY OF LIMITED STIMULUS, RESERVE BANK RATE (ROUGHLY EQUIVALENT TO FED. DISCOUNT RATE) WAS BEING LOWERED FROM 9 PERCENT TO 8.5 PERCENT. THIS WILL BRING BANK PRIME RATE DOWN TO 12 PERCENT. RESERVE BANK ALSO CUT THE LIQUID ASSET RATIO FOR SMALLER BANKS.

9. COMMENT: GIVEN THE UNCERTAINTY ON THE STRENGTH OF THE RECOVERY, IT WAS TO BE EXPECTED THAT THE GOVERNMENT WOULD RESTRICT ITSELF TO THE RATHER LIMITED MEASURES ANNOUNCED TO STIMULATE THE ECONOMY, ALTHOUGH THE PRIVATE SECTOR CONTINUES TO CALL FOR STRONGER MEASURES. THE RAPID RISE IN THE GOLD PRICE HAS GIVEN CONSUMER CONFIDENCE A BOOST AND PROBABLY IMPROVED THE OUTLOOK FOR SUSTAINED HIGHER CONSUMER EXPENDITURES IN SPITE OF THE SHARP JUMP IN PRICES IN JULY. HOWEVER, THE GOLD PRICE RISE IS ONLY IN TERMS OF DOLLARS, AND THE PRICE HAS SHOWN LITTLE INCREASE IN TERMS OF THE MARK AND THE YEN, BOTH CURRENCIES OF MAJOR SOUTH AFRICAN TRADING PARTNERS.

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WITH THE RAND LINKED TO THE DOLLAR, THE BALANCE OF PAYMENTS BENEFIT IS NOT PROPORTIONATE TO THE GOLD PRICE RISE, AND SOUTH AFRICA IS THUS NOT YET ABLE TO IGNORE THE BALANCE OF PAYMENTS CONSTRAINTS. THE MAIN CONCERN ON LOWERING INTEREST RATES HAS BEEN THAT IF THE GAP BETWEEN SOUTH AFRICAN AND OVERSEAS RATES WERE NOT MAINTAINED, SOUTH AFRICAN FIRMS WHICH NOW FINANCE MUCH OF THEIR TRADE WITH FOREIGN FUNDS WOULD SWITCH TO DOMESTIC SOURCES THUS INCREASING THE OUTFLOW OF SHORT-TERM CAPITAL. THE RESERVE BANK HAS APPARENTLY DECIDED THAT MOST COMPANIES WILL NOT RELINQUISH THEIR FOREIGN CREDIT LINES EVEN IF THE GAP IS CLOSED.

10. IN PRIVATE DISCUSSION EARLIER THIS MONTH, DEPUTY GOVERNOR OF RESERVE BANK DE KOCK FOUND IT DEMORALIZING THAT EXCELLENT TRADE RESULTS WERE NULLIFIED BY CAPITAL OUTFLOWS. ASIDE FROM REPAYMENT OF SHORT-TERM GOVERNMENT LOANS AND REDUCED TRADE CREDITS, HE ATTRIBUTED THIS TO MULTINATIONALS REPATRIATING EARNINGS PREVIOUSLY REINVESTED AND OTHER FINANCIAL MANIPULATIONS WHICH HAD EFFECT OF DISINVESTMENT.

11. DE KOCK WAS ENCOURAGED BY LOWER INFLATION RATE, BUT HE WAS CAUTIOUS ABOUT STRENGTH OF RECOVERY PENDING EVIDENCE OF SUSTAINED UPSWING IN CONSUMER SPENDING AND MANUFACTURING. FACT THAT INDUSTRIAL PLANT IS STILL OPERATING AT ONLY 84 PERCENT OF CAPACITY MEANT THAT LITTLE NEW INVESTMENT COULD BE EXPECTED.  
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## Message Attributes

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